

# FACTORING : PROBLEMS AND APPLICATIONS IN TURKEY

## MBA THESIS

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**FACTORING: PROBLEMS AND APPLICATIONS IN TURKEY**

**A THESIS**

**SUBMITTED TO THE FACULTY OF MANAGEMENT  
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**IN PARTIAL FULLFILMENT OF THE REQUIREMENTS  
FOR THE DEGREE OF  
MASTER OF BUSINESS ADMINISTRATION**

**By OĞUZ ÇANERİ  
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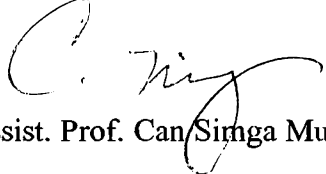
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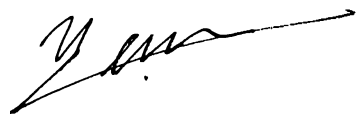
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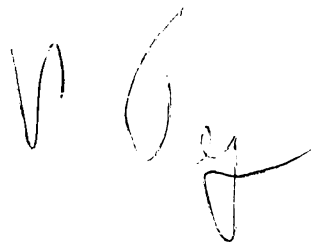
  
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*to my FAMILY*

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## **ABSTRACT**

### **FACTORING: PROBLEMS AND APPLICATIONS IN TURKEY**

**By**

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This study attempts to find out the problems of factoring in Turkey and come up with possible solutions. Factoring is introduced briefly by stating its functions, history and development in the world and Turkey. In addition, factoring is compared with Letter of Credit, Open Account, Cash Against Documents, Credit Insurance, Discount on Draft and Conveyance Credit. Moreover the problems of factoring in Turkey are stated and possible solutions are suggested. In this study it is found that factoring has superiority over other alternatives which Turkish firms prefer to use in their sales transactions. The study has also revealed that factoring is not regulated completely by the separate laws in Turkey. Finally, it is concluded that factoring is a financing technique that helps a lot in the development of trade of Turkey both in domestic and foreign markets. Expansion of factoring is inevitable which is fundamentally a good thing for the Turkish economy and for the factoring industry. Government and factoring firms should do everything to encourage that growth. Public acceptance of factoring is due to professional approach of factors.

**Keywords:** Accounts Receivable, Credit Management, Factoring, Factor, Factors Chain International, Financing Technique, Funding, Regulation.

## ÖZET

### FACTORING: TÜRKİYE'DEKİ PROBLEMLERİ ve UYGULAMALARI

Hazırlayan

Oğuz Çaneri

Tez Yöneticisi: Doç. Dr. Can Şımgı Mugan

Bu çalışma factoringin Türkiye'deki problemlerini belirleme ve bu problemlerin çözümü için gerekli değişiklikleri ortaya çıkarma amacındadır. Factoring, factoringin uygulamaları, tarihi ve gelişimi kısaca anlatılmaktadır. Bunun yanında factoring Türk firmalarının çoğunlukla tercih ettiği diğer finansman teknikleriyle de karşılaştırılmaktadır. Edilinen bulgulara göre factoring bu tekniklere göre daha avantajlı bir yöntemdir. Buna rağmen Türkiye'de factoringi tam anlamıyla düzenleyen ve işleyişini kolaylaştıran kanunlar bulunmamaktadır. Sonuçta factoringin Türk ticaretinin gelişmesine önemli katkıları olduğu belirlenmiştir. Factoringin yaygınlaşmasının kaçınılmaz olduğu ve bunun da hem factoring firmaları hem de Türk ekonomisi açısından olumlu etkileri olduğu anlaşılmıştır. Factoringin gelişmesi için devlet ve factoring firmaları ellerinden geleni yapmalıdır. Factoringin benimsenmesi büyük ölçüde Türk factoring firmalarının çabalarına bağlıdır.

**Anahtar Sozcukler:** Alacaklar, Kredi Yönetimi, Factoring, Faktor, Factors Chain

International, Finansman Yönetimi, Finansman, Düzenleme



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# CHAPTER I

## INTRODUCTION

Turkish firms are using several methods to ensure the receipt of payments for the goods and services they sell both in domestic and foreign markets. However, they usually face problems in collection of receivables arising from various transactions. This study aims to reveal that factoring has many advantages when compared to other alternatives. In addition, this study concentrates on the problems of factoring sector in Turkey and proposes several solutions for a well functioning factoring sector.

In every decade, there is a change in the fortunes of one or more of the different types of industrial and commercial finance. In 1950's the demand for finance for expansion of world industry was met largely by the banks through overdrafts and by the stock exchange through equity participation. In 1960's, finance companies led the way with the growth of industrial hire-purchase for productive equipment. Leasing companies were spectacularly successful in 1970's. Throughout the whole of the last thirty years, there is one group of financier who have grown quietly and steadily; the factoring companies. It is believed that end of 90's will see the explosion of factoring as the fastest growing financial facility in Turkey as it happened in most of the industrialized countries a decade ago.

It is mostly the small and medium scaled enterprises that prefer factoring. The amount of trade supplied by these companies constitutes a high percentage in Turkish economy. However, most of these firms do not believe in the benefits of factoring and prefer

traditional methods like Letter of Credit in their trade with other firms. Present study is believed to be useful in the sense that it both introduces factoring and shows its superiority to traditional methods. In addition, by proposing some solutions to problems faced by factoring firms, this study is believed to be a contributor to the development of a well functioning factoring sector. Factoring is gaining importance for both domestic and international trade of Turkey. Increase in Turkish trade will contribute to the solution of economic and social problems like unemployment and budget deficits. Since factoring is a facilitator of trade it should be well understood.

In Chapter 2, factoring is introduced briefly. The development of factoring in the world and Turkey is discussed with including the history of it and some statistical data. Also, information about Factors Chain International (FCI) is given in this chapter.

In Chapter 3, factoring is compared with some alternatives and advantages of factoring over these alternatives are shown. In this comparison letter of credit (LOC), open accounts, cash against documents, export credit insurance, discount on drafts and conveyance credit are included.

In Chapter 4, problems of factoring in Turkey are introduced and possible solutions to these problems are proposed. In addition, studies of factoring association in Turkey is included. The problems discussed are mainly the ones due to regulations and funding problems.

Chapter 5 is basically the conclusion section. Basics about factoring and problems of factoring are reintroduced in this section. In addition, future of factoring for Turkey is discussed and recommended actions are provided.

## CHAPTER II

### OVERVIEW OF FACTORING

#### DEFINITION AND DESCRIPTION OF FACTORING

##### What is Factoring?

Factoring is defined as the transfer of receivables of a firm to a factor and collection of payments for receivables by the factor. The business entity obtains short term financing through factoring; that is it speeds up the turnover of receivables into cash. In addition the seller puts its receivables under guarantee since the factor takes the risk of default of payments. Moreover, the seller is freed from routine tasks such as collection of payments and following of receivables.

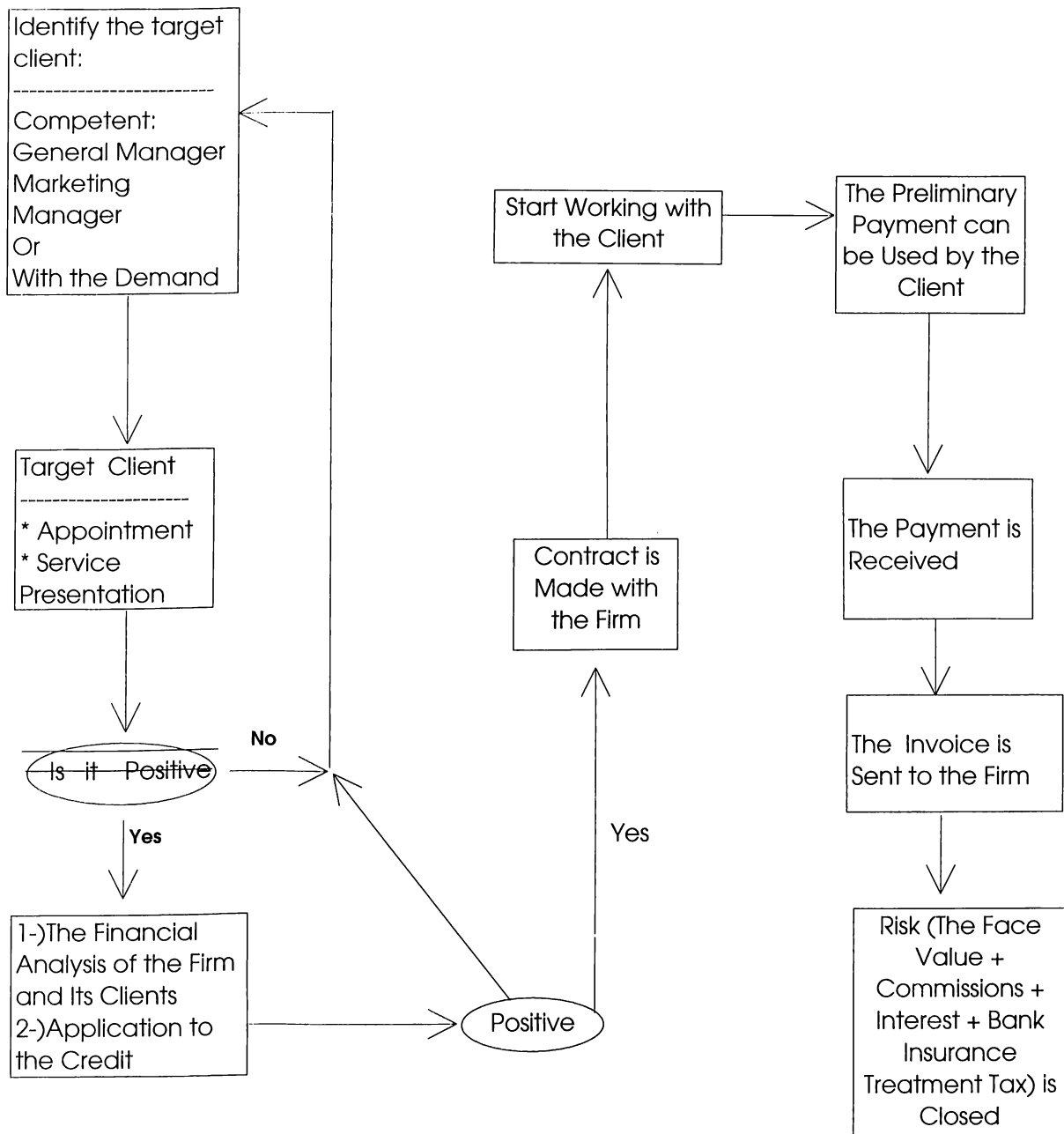
Cost of funding for the firms which work mainly with foreign resources increases especially in crisis times because of increasing interest rates. Factoring gains importance as a financing alternative in an environment in which banks demand a lot when giving credits. Factoring helps firms which their products in the domestic market in forward with long maturity and export firms which are not familiar with foreign buyers. Factors are lifeguards especially in the times of crisis because they take all or part of the risks the seller faces.

## **How is factoring conducted?**

### **Domestic Factoring**

There are three entities in domestic factoring: Seller (client), buyer (debtor) and factoring firm (factor). Seller applies for the factoring operation to the factor. Factor meets with the seller to find out its financial position and demands a report including the list of debtors and planned sales to the debtors. Factor obtains information about the debtors. After the negotiations between the seller and the factor, factoring agreement is signed. Commissions of the factor, interest rate and other conditions are included in the contract. Factor informs the seller about the guarantee limits determined for each debtor. Seller informs the factor with a letter that the factoring operation has started and sends the invoice for the goods sold. After the goods are shipped the invoice is sent to the buyer. On a copy of the invoice, a conveyance note specifying that the seller transferred the right for the receivables to the factor and that the payment will be made only to the factor, is written. A copy of the invoice with the conveyance note and a copy of the loading document is sent to the factor. After these steps the seller transfers the receivable to the factor within the scope of the factoring agreement and the risk for the payments is borne by the factor. With the demand of the seller, the factor pays up to %80 of the debt to the seller with cash. The remaining amount, from which the agreed interest and commissions are deducted, is paid on maturity date. The flow chart for domestic factoring can be seen in Figure I.

**FIGURE I**  
**DOMESTIC FACTORING FLOWCHART**



Source: Euro-Factoring Marketing Department



## **Export Factoring**

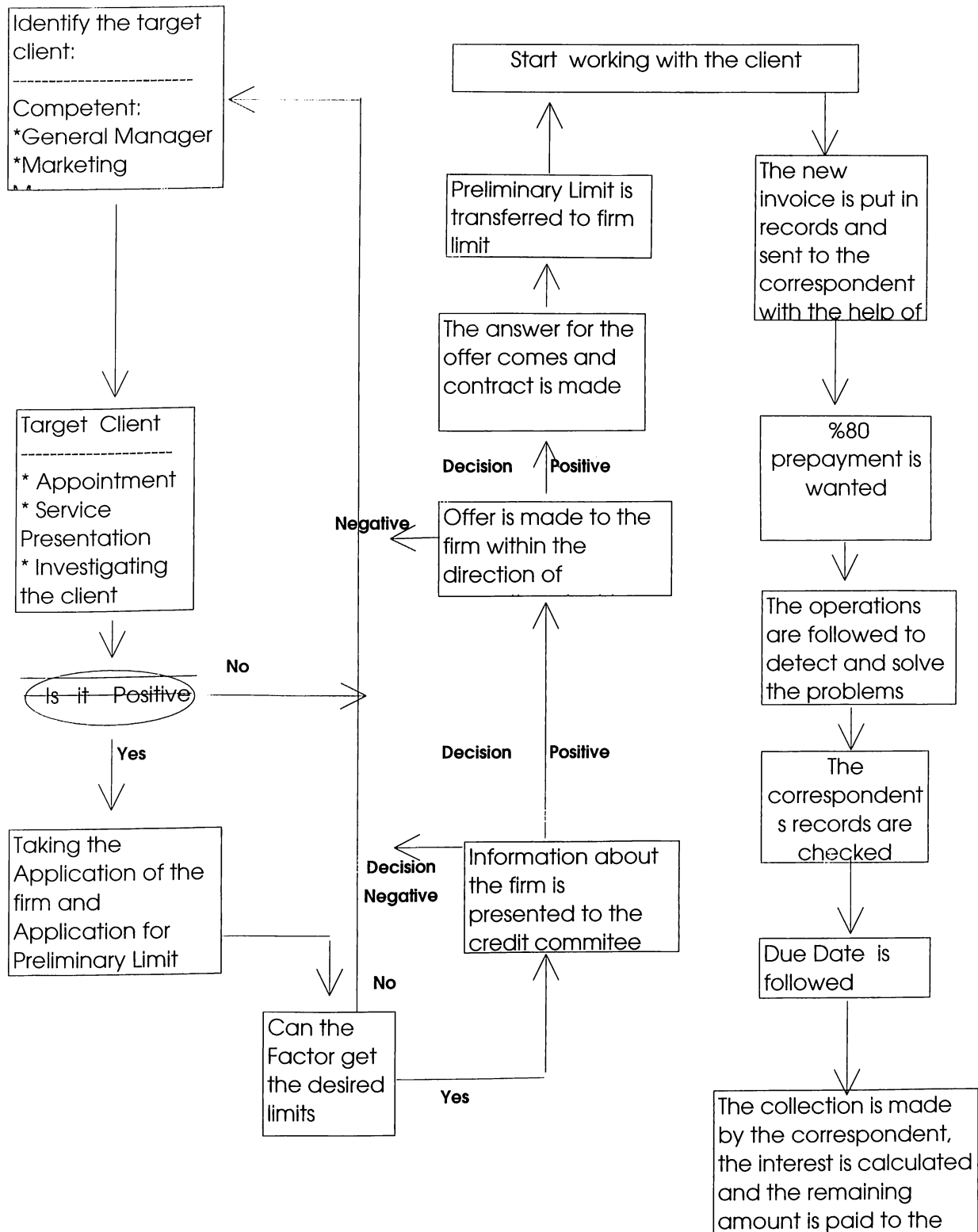
The export firm is released from the foreign credit risk by export factoring. In addition, it is saved from the problems like exchange rate risks, different regulations and trade information about the market. Drawee of the seller in export factoring for the receipt of payments, provision of financing and risk taking, is the factor in the seller's country.

There are four entities in export factoring: Seller(exporter), buyer(importer), factor and the correspondent factor in the importer's country. Seller gives the information about the buyer to the factor after the buyer orders the goods. Factor obtains further information about the buyer through the correspondent factor and tells the guarantee limits determined by the correspondent factor to the seller. Factor provides %100 guarantee within these limits in case that the buyer does not pay its debt or the buyer faces financial problems. Seller ships the goods and sends the invoice to the buyer. A copy of the invoice with the conveyance note is sent to the factor. Factor pays up to %80 of the invoice in cash with the demand of the seller. A copy of the invoice is sent to the correspondent factor. On due dates of the debts correspondent factor collects the payments and sends them to the factor in the seller's country. The factor pays the remaining amount to the seller after deducting the commissions and the interest. The flow chart for export factoring can be seen in Figure II.

## **Functions of Factoring**

Factor provides various services for the needs of the clients. The services are collected under three main headings.

**FIGURE 11**  
**EXPORT FACTORING FLOWCHART**



Source: Euro-Factoring Marketing Department

#### Financing:

The factor pays up to %80 of the amount in invoice in cash with the demand of the seller. In this case, a copy of the invoice and the loading document are sent to the factor. If the invoice amount is within the credit limits approved for the buyer, factor makes the payment. The remaining net amount is paid after the debt is received and the commissions of the factor are deducted. With this method the turnover of receivables into cash becomes faster and the seller's need for cash to finance the sales with credit is satisfied.

#### Collection of Debt and Accounting:

The factor deals with specifying the creditworthiness of the buyer and the receipt of payments from the buyer. The factor also deals with book keeping and accounting for these receivables. In order to provide this service, the factor wants a copy of the invoice sent by the seller and receives the payments from the buyer. Thus, the seller is saved from routine tasks like accounting of receivables and can concentrate more on its main duties; production and marketing. In addition, collection is made on time and in order, due to the factoring firm's excellent collection policy.

#### Credit Management:

Factor puts the receivables of the seller under guarantee by taking the risk of non-payment by the buyers. In case that the buyer has problems in payment or the buyer does not pay, the debt is paid to the seller 90 days after maturation. Thus, factor undertakes and manages the receivables account of the seller.

These three services are either offered together or with the demand of the clients offered separately.

## FACTORS CHAIN INTERNATIONAL

Factors Chain International (FCI) was established in 1968 as an open factoring chain by an independent group of European factors. In the establishment stage, FCI put forward that market strengths and competition should be the determining factor for the success of its members in a country.

The key factor that contributed to the development of FCI was the transfer of know-how and experience from settled factors to ones with less experience. This transfer occurs in several forms. The most known ways are seminars, meetings, courses and visits made by the members to each others establishments. The more formal way of this transfer is the transfer of operational rules and FCI code between members.

FCI is a foundation established by the big factors in Holland which have the common aim of conducting international trade through factoring and related financial services. It is established in order to form a global communication network between factors. FCI helps its members to gain competitive advantage through :

- 1- Modern and efficient communication network which helps factors to conduct operations with suitable costs
- 2- A legal framework which protects importers and exporters
- 3- Standard procedures with the aim of creating universal quality
- 4- An education programs package
- 5- Development of factoring in the global arena.

There are two kinds of FCI membership; full membership and associated membership. The factoring firm accepted as a member is regarded as an associated

member in the beginning. It is required that associated members should realize at least \$5 million factoring volume per year to stay as a member. After this member remains as an associated member for two years and its operations volume through correspondent factors becomes at least \$10 million per year, it can acquire the right to be a full member. In addition the minimum capital for these factors should be at least \$1 million.

The difference between full members and associated members is that full members have more power in the organization. When a conflict arises between a full member and an associated member, Factors Chain International will be more inclined to take the side of the full member in calming down the conflict. The complete list of associate and full members of FCI can be seen in Table I-A in the Appendix.

### **Administration of FCI**

**Council:** It is the most authorized office and includes all the full members.<sup>1</sup> Council elects the Administrative Committee and the head of Board of Directors.

**Administrative Committee:** It conducts regular meetings, approves new members and forms the Technical Committee.

**Technical Committee:** These are established for evaluation of a subject in a period or continuously.

These duties are supported by Legal, Marketing, Communication and Education Committees. The secretariat in Amsterdam is responsible for daily activities. The head of

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<sup>1</sup>Other members which do not have full membership have limited voting rights

this secretariat is the General Secretary and is appointed by the Administrative Committee.

There are 120 members of FCI in 43 countries. These members help each other in international trade activities. FCI developed a communication network named EDIFACTORING (Electronic Data Interchange for Administration, Commerce and Transport) for its members. The main aim of the system is the exchange of information through electronic methods. EDIFACTORING is used by all FCI members since May 1994.

In 1994, the international factoring volume for FCI members was about 10 billion USD. This is %22 more when compared with the previous year. The total volume of domestic and international factoring for FCI members increased by %17 and reached up to 130 billion USD. This means a market share of %44 of the factoring sector. In 1994, FCI members gave factoring services to 52000 clients.

Volume of export factoring is still smaller when compared with domestic factoring. However, the growth rates of export factoring in the last 6 years is higher than the growth rate for domestic factoring. The important markets in this area are West Europe, USA, Japan, Hong Kong, Korea, Taiwan and Singapore. Among the new markets for international factoring are China, India, Russia, Greece, Poland and in recent times Argentina and Chile.

FCI and members help firms to enter into new markets and facilitate trade in present markets. The members will increase because FCI aims to have members in all countries.

## HISTORY OF FACTORING

It is believed that Romans were the first to pass on a formal instrument of credit by issuing promissory notes at a discount. A more formal illustration is the Pilgrim's journey to America. The Pilgrims received their original authorization for settlement in America from the London Company<sup>2</sup>. This organization was a joint stock company comprised of London merchants who expected to receive a reasonable return on their investment in America because of its vast resources.

Since the Pilgrims did not have substantial capital to finance their immigration to America, they negotiated an agreement with a London factor named Thomas Weston. The London iron merchant advanced moneys for repayment at a future date against the Pilgrim's accounts receivables, which were the raw materials the colonists would ship to London. The factor would then sell the colonial materials. However, he would probably sell the receivables at a great discount because of the high risk involved with transporting and receiving the raw materials from America. In essence the factor guaranteed the colonial purchasers credit to and collected debts for the London merchants who exported goods to the colonies.

After the industrial revolution the factor became more of a banking and credit servicing entity; in that the factor assisted in approving customers and credit limits, guaranteed payment for approved customers and then purchased its clients bad debts. As trade developed on a larger scale, credit was needed to finance shipments of goods thereby augmenting the need for factors.

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<sup>2</sup>Actual name was the Virginia Company of London

It is accepted that the history of modern factoring started in 1890's in United States of America. In this respect, the Mc. Kinley Customs Tariff was a turning point. With this tariff the export of European textiles to America was impeded. As a result, the American factors, who undertook the sales of European textile products and collected the payments, lost their markets. Then, these factors started conducting their jobs in the domestic market. However, there was no need for stocking and sales assistance in the domestic market. So, the American factors started offering services like collection of payments in the domestic market, taking up the risk of non-payment and provision of financing. Thus modern factoring was started in US.

After the Second World War, American factoring banks started carrying their operations to European countries. After 60's modern factoring started being implemented in Europe with the help of American factors. The first factoring operation in Germany was conducted in 1958. Then factoring started being used in countries like Austria, Switzerland, France, Belgium, Holland and Sweden. After 70's factoring started being used in Japan and other East Asian countries like Singapore, Hong Kong, Taiwan and South Korea. The first factoring firm in Japan was established in 1972 with contributions of an American bank.

After 1984, major developments took place in Turkish banking system. In the mid of 1988, the first unit dealing with factoring was established. In their first years factors in Turkey were dealing only with exports and sometimes with imports. After 1991, factoring started being used in the domestic market. The number of factoring firms and total factoring volume in Turkey with years are in Table I.



**TABLE I**  
**NUMBER OF FACTORING FIRMS AND TOTAL**  
**FACTORING VOLUME IN TURKEY**

YEAR	VOLUME (Million \$)	NUMBER OF FACTORING FIRMS
1988	3	4
1989	16	1
1990	65	4
1991	190	5
1992	600	25
1993	900	100

Source: Finans, May 1995

In 1994 there was a decrease both in factoring turnover (in USD) and the number of factoring firms in Turkey. However, in 1995 factoring was recovered and turnover started to increase.

## DEVELOPMENT OF FACTORING

### Development in the World

The fast growth of international trade after 70's, open economic policies of developing countries and their desire to construct their economies caused the development of various financing techniques. Among these techniques that provide funds for foreign trade operations, guarantee collection of receivables, and aim to create new markets for products, factoring gained importance.

By the end of 1985, there were 299 factoring firms in the world which created a factoring volume of \$85 billion (Table II). In 1993, total factoring volume reached up to \$260 billion. By the end of 1994 there were 597 factoring firms and the total volume was \$294 billion. In the period 1985-1994 number of factoring firms almost doubled and the total factoring volume increased by %250.

**TABLE I I**

**WORLD FACTORING VOLUME**

YEARS	NUMBER OF FIRMS	FACTORING VOLUME (Million \$)
1985	299	85300
1988	416	160186
1990	507	244327
1991	662	266000
1992	810	264309
1993	890	260844
1994	597	294926

Source: Dunya, August 21, 1995

The distribution of world factoring volume is shown in Table III. Europe <sup>3</sup> is the first in this comparison. When we consider the countries individually, the US is the first and Italy is the second (Table IV) in factoring volume. <sup>4</sup> The number of factoring companies is highest in Italy. <sup>5</sup> A detailed analysis of factoring volume and number of factoring companies by countries is found in Table V.

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<sup>3</sup> Total of all European countries

<sup>4</sup> Both in Domestic and Export Factoring

<sup>5</sup> There are 70 factoring companies

**TABLE III****WORLD FACTORING VOLUME (Million \$/1994)**

	Number of firms	Domestic	Export	Total
Europe	324	152820	15679	168499
United States	86	76920	2070	78990
Africa	12	1740	70	1810
Asia	159	41893	2124	44017
Australia	16	1520	90	1610
TOTAL	597	274893	20033	294926

Source: Dünya, August 21 1995

**TABLE IV****FIRST TEN COUNTRIES IN FACTORING VOLUME (Million \$/1994)**

	Number of firms	Domestic	Export	Total
USA	14	57900	1700	59600
Italy	70	44170	1600	45770
England	40	42000	1300	43300
France	29	21900	2100	24000
Japan	43	23058	745	23083
S.Korea	34	13700	550	14250
Mexico	47	13500	200	13700
Germany	16	10000	2000	12000
Holland	5	5225	5225	10450
Spain	20	4850	280	5130

Source: Ekonomi, August 21, 1995

TABLE V

FACTORING	TURNOVER	BY COUNTRY IN	1994 IN MILLIONS OF USD	
EUROPE	Number of firms	Domestic	International	Total
Austria	3	1850	180	2030
Belgium	7	3440	1560	5000
Cyprus	2	305	25	330
Czech Rep.	5	150	150	300
Denmark	7	2200	300	2500
Finland	5	2300	30	2330
France	29	21900	2100	24000
Germany	16	10000	2000	12000
Greece	4	0	15	15
Hungary	8	70	50	120
Iceland	1	0	25	25
Ireland	4	2100	30	2130
Italy	70	44170	1600	45770
Netherlands	5	5225	5225	10450
Norway	8	4465	200	4665
Portugal	10	2700	85	2785
Romania	1	0	4	4
Russia	1	0	0	0
Slovakia	1	25	25	50
Slovenia	1	0	5	5
Spain	20	4850	280	5130
Sweden	15	4000	150	4150
Switzerland	1	420	120	540
Turkey	60	650	220	870
United Kingdom	40	42000	1300	43300
	<b>324</b>	<b>152820</b>	<b>15679</b>	<b>168499</b>
AMERICA				
Brazil	-----	3500	0	3500
Canada	17	1630	160	1790
Chile	5	300	10	310
Colombia	2	40	0	40
Ecuador	1	50	0	50
Mexico	47	13500	200	13700
U.S.A.	14	57900	1700	59600
	<b>86</b>	<b>76920</b>	<b>2070</b>	<b>78990</b>
AFRICA				
Morocco	3	40	20	60
South Africa	9	1700	50	1750
	<b>12</b>	<b>1740</b>	<b>70</b>	<b>1810</b>
ASIA				
China	4	0	40	40
Hong Kong	4	260	300	560
Indonesia	25	500	25	525
India	3	160	0	160
Japan	43	23058	745	23803
Malaysia	15	1560	60	1620
Philippines	2	35	5	40
Singapore	20	1700	200	1900
South Korea	34	13700	550	14250
Sri Lanka	2	15	0	15
Taiwan	1	0	194	194
Thailand	6	905	5	910
	<b>159</b>	<b>41893</b>	<b>2124</b>	<b>44017</b>
AUSTRALASIA				
Australia	15	1500	90	1590
New Zealand	1	20	0	20
	<b>16</b>	<b>1520</b>	<b>90</b>	<b>1610</b>
TOTAL WORLD FACT.VOLUME	<b>597</b>	<b>274893</b>	<b>20033</b>	<b>294926</b>

Source: İktisat Bankası

There has been a considerable increase in total factoring volume of FCI members in the last 25 years. While the total factoring volume of FCI members was \$3.9 billion in 1969, it became \$6.8 billion in 1974, \$16.2 billion in 1979, \$19.4 billion in 1984, \$80.5 billion in 1989 and \$130.2 billion in 1994. In 1994, FCI members realized almost half of the world factoring volume. Table VI shows the accumulative turnover figures for all FCI members compared to worldwide factoring turnover.

**TABLE VI**  
**ACCUMULATIVE TURNOVER FIGURES FOR ALL FCI MEMBERS**  
**COMPARED TO WORLDWIDE FACTORING TURNOVER (Million \$)**

	USD	USD	USD	USD	USD	INCREASE
	1990	1991	1992	1993	1994	94/93
Invoice Discounting	12989	13987	13354	14228	15149	6.47%
Recourse Factoring	31710	32661	33907	31713	27782	-12.40%
Non Recourse Factoring	41662	44137	45426	47815	66159	38.36%
Collections	5748	6813	7569	9079	11201	23.37%
Total Domestic Factoring FCI	92109	97598	100256	102835	120291	16.97%
Export Factoring	4207	4433	4017	4848	5867	21.03%
Import Factoring	2622	2506	2634	3225	4008	24.26%
Total International Factoring FCI	6829	6939	6651	8073	9875	22.32%
<b>Grand Total FCI</b>	<b>98938</b>	<b>104537</b>	<b>106907</b>	<b>110908</b>	<b>130166</b>	<b>17.36%</b>
World Domestic Factoring	230564	250626	249914	246288	274893	11.61%
World International Factoring	13763	15744	14895	14556	20033	37.63%
<b>World Total</b>	<b>244327</b>	<b>266370</b>	<b>264309</b>	<b>260844</b>	<b>294926</b>	<b>13.07%</b>

Source: Euro Factoring Training Notes

In Table VII, it is seen that total world volume of domestic factoring is much more than volume of international factoring. However, it is believed that as more developing countries enter the global arena, the volume of international factoring will increase.

**TABLE VII**

**WORLD FACTORING VOLUMES(BILLION \$)**

	EXPORT	DOMESTIC	TOTAL
	FACTORING	FACTORING	FACTORING
1990	137	2305	2442
1991	157	2506	2663
1992	148	2494	2642
1993	145	2463	2608
1994	20	2748	2949

Source: Ekonomi, June 1995

**Development in Turkey**

Turkey's open economic policy prepared the development conditions of factoring. In 1988, there were 4 factoring firms and the factoring volume was \$3 million.(Table I) However, by the end of 1993, the number of firms increased up to 100 and the total volume increased to \$900 million. Among these factors there were the ones established just for lending money. So, with the regulations in 1995, the number of factors that were qualified to be a factoring firm decreased to 44. The name and amount of capital of the factoring firms in Turkey can be seen in Table VIII. As in other countries, domestic factoring is used more extensively than international factoring as seen in Table IX.

**TABLE VIII**

**FACTORING COMPANIES IN TURKEY**

<b>Factorina Companies</b>	<b>Establishment Date</b>	<b>Capital (billion TL)</b>
Acar Factoring A.S.	2.2.1993	75
Ak Factoring Hizmetleri A.S.	-	75
Akdeniz Factoring Hizmetleri A.S.	22.6.1993	75
Aktif Finans Factoring Hizmetleri A.S.	19.6.1990	189
Atlas Factoring Hizmetleri A.S.	6.8.1993	75
Baser Factoring A.S.	5.7.1995	75
Best Factoring A.S.	10.8.1993	75
Cagdas Finans Factoring Hizmetleri A.S.	-	75
Demir Factoring A.S.	23.6.1993	100
Devir Factoring Hizmetleri A.S.	14.5.1991	75
Dis Factoring A.S.	25.11.1992	75
Ege Factoring Hizmetleri A.S.	11.2.1994	75
Eko Finans Factoring Hizmetleri A.S.	23.3.1994	75
Ekspres Factoring A.S.	27.8.1993	150
Endeks Factoring ve Finansman A.S.	14.2.1994	75
Era Finans Factoring A.S.	24.8.1992	105
Es Facto Factoring Hizmetleri A.S.	27.8.1992	75
Facto Finans Alacak Alim-Satimi Hizmetleri A.S.	5.6.1990	120
Facto Kapital Factoring Hizmetleri A.S.	2.8.1993	75
Ferman Factoring A.S.	-	75
Fiba Factoring Hizmetleri A.S.	27.11.1992	100
Fon Factoring Hizmetleri A.S.	26.10.1993	75
Genc Factoring Finansal A.S.	-	75
Heller Factoring A.S.	11.2.1992	228
Hepkon Factoring Hizmetleri A.S.	6.8.1992	75
Istanbul Factoring Hizmetleri A.S.	22.6.1993	75
Is Factoring Finansal Hizmetler A.S.	6.7.1993	75
Kapital Factoring Hizmetleri A.S.	22.5.1993	75
Katmerci Factoring Hizmetleri A.S.	-	75
Kulevoglul Factoring Finansal Hizmetleri A.S.	29.11.1993	75
Kura Factoring Finansal Hizmetler A.S.	4.10.1993	75
Kurtulus Factoring Hizmetleri A.S.	13.1.1993	75
Oz Finans Factoring Hizmetleri A.S.	15.6.1992	75
Pamuk Factoring A.S.	30.9.1992	75
Reel Factoring A.S.	5.4.1994	75
Setat Factoring A.S.	29.9.1992	75
Sirinoglu Factoring Finansal Hizmetleri A.S.	28.12.1992	75
Tekstil Factoring Hizmetleri A.S.	3.3.1994	75
Toprak Factoring A.S.	13.5.1994	75
Tutun Factoring Hizmetleri A.S.	-	75
Ticaret Factoring Hizmetleri A.S.	16.7.1993	75
Tur Factoring Hizmetleri	11.1.1993	75
Ulus Factoring A.S.	12.8.1992	75
Umur Ture Finans Factoring Hizmetleri A.S.	14.9.1993	75
<b>Bank's Subsidiaries:</b>	<b>15</b>	
<b>Other</b>	<b>29</b>	

Source : Undersecretariat of Treasury

TABLE IX

FACTORING VOLUMES FOR TURKISH FACTORS (Million \$)

	1994	1993	1992	1991	1990
Export Factoring	220	270	167	128	56
Domestic Factoring	650	700	287	55	6
Total	870	970	454	183	62

Source: Ekonomi, May 1995

When we compare Turkey with other countries in factoring volume (Table V) we see that it is in the bottom part of the range. The reasons for this finding is that factoring has not been widely accepted by Turkish firms since its benefits are not communicated to them, it is faced with problems in application and there has been some economic problems in the country.

In 1993, the total factoring volume of Turkey was \$970 million. However, we see a decrease in this amount in year 1994. While the world factoring volume increased by %20 in the same year, there was a decrease in Turkey. There was an economic crisis in the country which caused a huge devaluation of Turkish lira against the US dollar. Since exchange rate risk was high there was a decrease in foreign trade and since buying power of TL decreased because of high inflation domestic demand soared in 1994. As a result there was a decrease in trade of Turkish firms and hence in demand for factoring.

Table X shows factoring usage by sectors. In Turkey (by the end of 1995), factoring facilities is preferred more by the industry sector than the services sector. The food sector is the first and the textile sector is the second in cumulative factoring transaction volume. In each of these sectors domestic factoring volume is much more



than export factoring volume. In services sector, the volume is highest for trade and construction services. In this sector firms export factoring volume is too low.

**TABLE X**

**CUMULATIVE FACTORING TRANSACTION VOLUME IN TURKEY (MILLION TL)**

July 1st-Sept. 30th 1995	Domestic	Export	Total
<b>SECTORS</b>	<b>Factoring:</b>	<b>Factoring:</b>	
<b>INDUSTRY</b>	<b>7.708.180</b>	<b>2.546.633</b>	<b>10.164.813</b>
Textile	1.788.659	1.414.657	3.203.316
Food	2.819.733	804.463	3.624.196
Automotive	325.185	3.385	328.57
Durable Consumer Goods	19.379	150.335	169.714
Office Equipment	97.926	17.791	115.717
Machine,Equipment, Spare Parts	1.232.541	112.479	1.345.020
Chemistry	756.734	43.524	800.258
Paper and Other Paper Products	493.612	0	493.612
Other	1.760.891	852.245	2.613.136
<b>SERVICES</b>	<b>2.946.882</b>	<b>384.558</b>	<b>3.331.440</b>
Trade	1.132.015	337.023	1.469.038
Tourism	44.804	0	44.804
Education	14.539	0	14.539
Health	202.644	3.164	205.808
Transportation	280.162	44.371	324.533
Construction services	1.001.244	0	1.001.244
Broadcasting	145.771	0	145.771
Other services	126.103	0	126.103
<b>OTHER</b>	<b>327.191</b>	<b>0</b>	<b>327.191</b>
<b>TOTAL</b>	<b>10.982.253</b>	<b>2.931.191</b>	<b>13.913.444</b>

Source: Undersecretariat of Treasury

## **CHAPTER III**

### **COMPARISON OF FACTORING WITH ALTERNATIVES**

#### **FACTORING VS. LETTER OF CREDIT(LOC)**

Today, guaranteeing exports is the most widely used method in international trade. Sales made to foreign countries can become a bad experience. These kind of sales have additional risks, like exchange rate risk and insufficient information about foreign buyers, for small firms. The problem for the exporters is whether the buyers will make payment after the goods are shipped. This problem is more important for Small and Medium Scaled Enterprises (SME) because most of these firms do not have enough resources to finance sales in forward. Sales made to foreign firms can cause huge losses for SMEs. Exporters insist on the most dependable trade conditions in order to overcome this problem. Most exporters think that letter of credit is the suitable solution for the risk of nonpayment of debts by the buyers. Exporters give up the sales to the client in case that the conditions of letter of credit are not satisfied.

Firms conduct sales to foreign firms through letter of credit as follows: (Figure III)

1- Importer communicates the bank, it conducts business with, the necessary conditions for preparation of letter of credit text.

2- After the importer's bank prepares the letter of credit, it sends it to the correspondent bank in the exporter's country.

3- The correspondent bank notifies the exporter in the letter of credit that the suitable documents should be prepared.

4- The exporter ships the goods while preparing the suitable documents. The documents include: Invoice, bill of lading, certificate of origin, customs exit document, supervision document and other necessary documents. The goods should have been shipped for the preparation of documents.

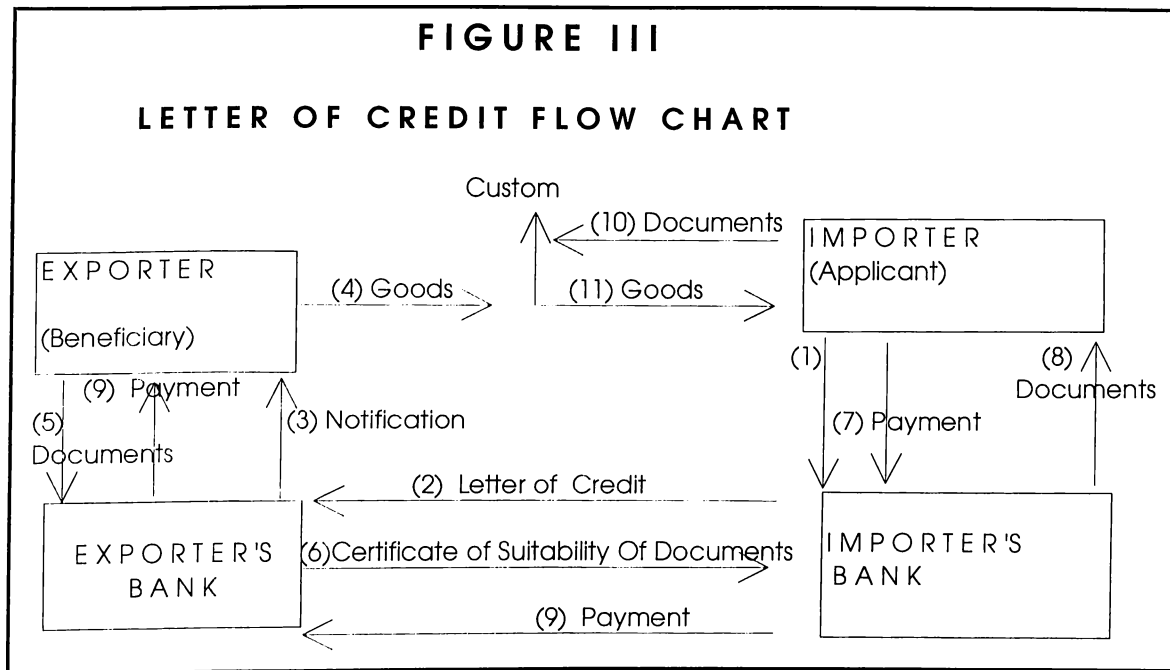
5- Exporter gives the documents to its bank. If there are missing parts in the documents, the bank wants the exporter to complete them because even a comma error in the letter of credit can be a cause for reserve on the letter.

6- Exporter's bank sends the certificate of suitability of documents and the documents to the importer's bank.

7-8 Importer makes the payments and gets the documents.

9- Importer's bank makes payment to the exporter's bank.

10-11 Importer gives the documents and gets the goods from customs.



Source: Iktisat Bankasi

When factoring and letter of credit are compared, factoring has the following advantages:

- With all types of letter of credit there is the probability that the importer will not take delivery of goods and will not make the payment although the exporter has already shipped the goods. However, there is no risk for unacceptance of goods with factoring since bill of loading is written in name of the buyer. This means that the goods become the property of the buyer. In case that the buyer decide not to get the goods and hence do not make the payment, there will be no loss for the seller because factor bears the risk of nonpayment. The buyer will probably make the payment to the factor in due date. Nonpayment will have bad effect on the creditworthiness of the buyer. Factor, through its relations with banks and factoring firms, communicates this case in the trade market. As a result, the reputation of the seller will be affected and this can cause even the bankruptcy of the seller.

- There is always the probability that the importer can put reserve on the letter of credit because of a missing document or unsuitability of the LOC text and hence can cause problems for the exporter.<sup>1</sup> However, this can not happen in factoring <sup>2</sup> and the exporter gets its money at most 90 days after maturity. In factoring, the exporter is not responsible for the errors that would occur in documents
  
- The imports made by letter of credit lessens the credit limit for the importer from the banks and it becomes harder for the importer to enter into new transactions.
  
- For each sales and for each loading, a new letter of credit should be opened. Usually delays occur when opening a letter of credit. This causes a loss of time and at the same time is not suitable for sales that are small, that require repetition of procedures and that require quick delivery. However, factoring firms try to form a long lasting relationship with the buyers. Buyers become the client of the factor and the contract is valid for the future transactions. The only thing that can be changed in the contract is the credit limit set by the factor.

## **Result**

As seen factoring has advantages for both importers and exporters. The use of letter of credit depends on the trust of parties on each other. One of the parties, with bad intentions or because of difficulties arising from the operations, can enter into negative behavior in order to cancel the transaction. Such behavior wears out the trade and

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<sup>1</sup> The importer can do this with bad intentions

<sup>2</sup> In case that the error does not arise from the exporter

lengthens the transaction time. At the same time, commissions paid by both importers and exporters to the banks that act as intermediaries increase.

The importer has the right to declare that the goods shipped do not satisfy the requirements of the transaction. The buyers can declare such things on purpose when they face difficulties of payment. However, a seller who conducts business through factoring is not effected from such acts because it has already received the payments.

In case that the goods do not meet the necessary specifications and that it is the fault of the seller; the seller is responsible for compensating the losses of the buyer.

### **Comparison of Costs of Factoring and Letter of Credit:**

When LOC is opened, the importer pays commission and tax to the banks. The rate of commission and tax changes according to creditability of the importer, the country of origin of the importer and the maturity of the debt. In Turkey, commissions taken from the importer are %0.4-%0.6 on the average. These rates decrease to %0.1-%0.2 for big importers. If there is no subsidy for the imported good, %0.6 Stamp Tax and %0.1 Expense Tax is taken. So for a medium sized firm (having sales of 500-600 billion TL) the total cost of letter of credit is;  $\%0.5 + \%0.6 + \%0.1 = \%0.12$  of the value of sales.

In LOC the costs are taken from the importer while they are taken from the exporter in case of factoring. In LOC the cost for the exporter is 0. It pays a commission of %1-%1.5 in case of factoring. However, the exporter transfers some or all of this cost to the importer.

The maximum difference between the cost of factoring and letter of credit is %1.5 - %1.2 = % 0.3 of the sales made. The cost of factoring can decrease down to %1 of sales made. However, as cost decreases the risk covered by the factoring agreement also decreases.

More information about factoring interest rate, commission, maturity, advance rate and amount of checks and promissory notes received as guarantee in the period of July-September 1995 can be seen in Table II A in the Appendix.

### **FACTORING VS. OPEN ACCOUNT**

In open account exporting, seller trusts on the buyer. Export is done as open sales and the payment is done as put forward <sup>3</sup>. In this kind of sale, there is no guarantee of payment for any party. Although there is the trust of parties on each other there is no guarantee for the seller in case of bankruptcy of the buyer. In exports with open accounts, it is seen that the buyer and the seller have been working for a long time. Previously they work with Letter of Credit or with Cash Against Documents but after trust is formed they use the method of Open Account to benefit from its facilities.

Open Accounts is more advantageous for importers. The importer is under no obligation and it can use the credit line, which would otherwise be tied to this purchase, in another transaction.

Open account export transactions work as follows:(Figure IV)

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<sup>3</sup>Paid in advance, in forward etc.

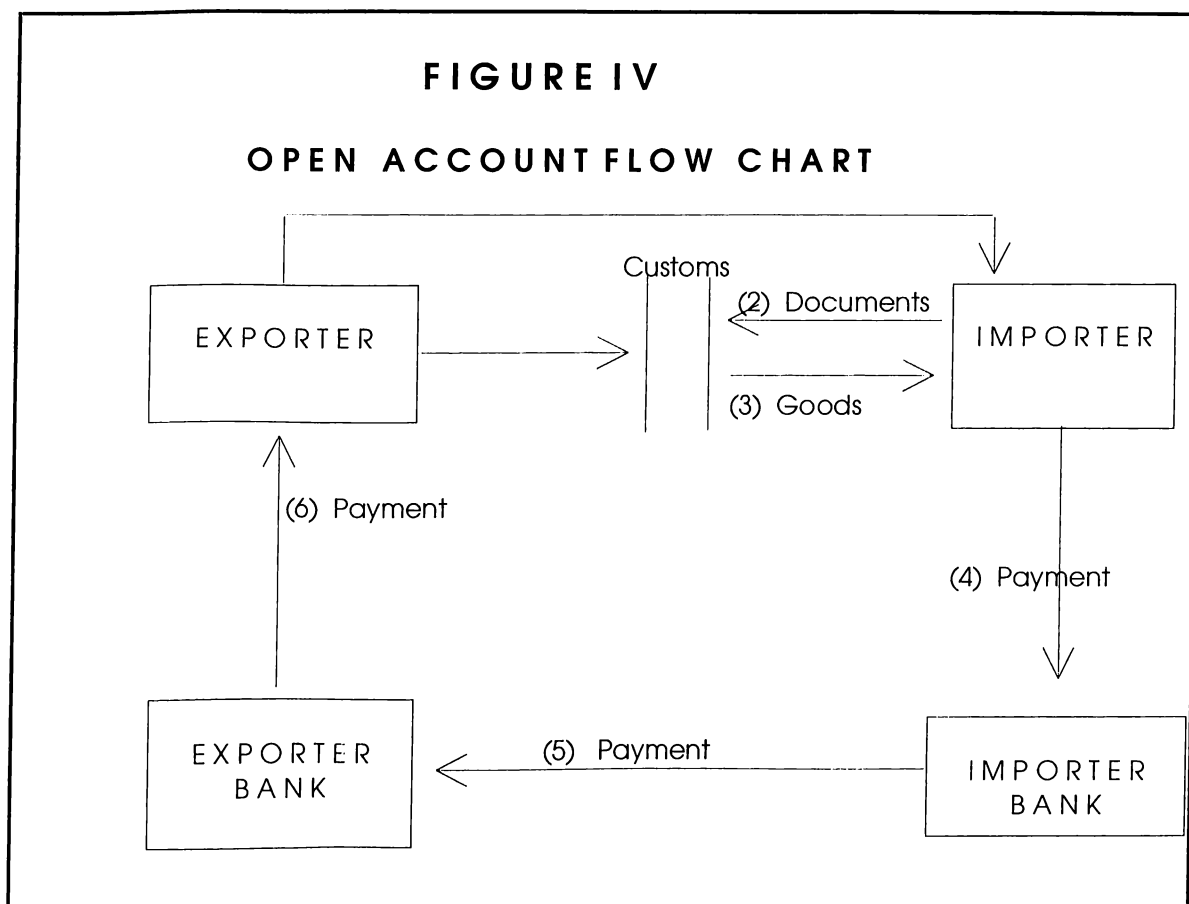
1- Exporter sends the goods ( the documents are sent to the importer through the bank or with the goods)

2-3 The importer takes the goods from the customs with the document in hand

4- Importer makes the payment in due date

5- Importer's bank transfers the amount to the exporter's bank

6- Exporter's bank makes the payment to the exporter



Source: Iktisat Bankasi



## **Open Accounts with Acceptance Credit**

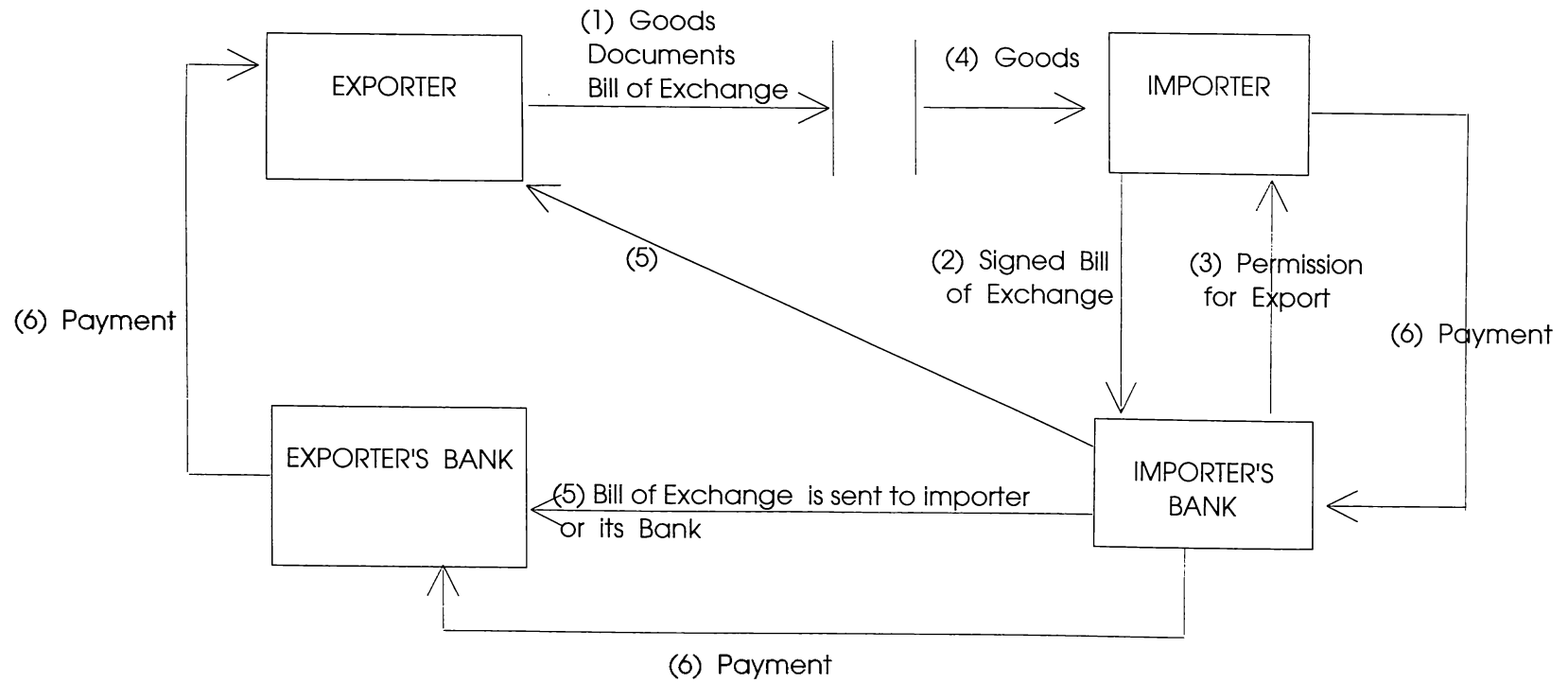
In addition to the goods and documents, a bill of exchange is also sent to the importer. The difference of this method from Open accounts is as follows: There is trust between parties (open account is made); at the same time there is fixed term and an exchange deed. The acceptance credit is given by the importer's bank. If the bank guarantees, bill of exchange can be turned into cash through forfaiting. The reason for conducting the export through this way is this advantage of turning bill of exchange into cash before maturity.

As in Figure V, The Open Account with Acceptance Credit works as follows:

- 1- Goods, documents and bill of exchange is sent to the importer
- 2- Importer signs the bill of exchange and gives it to the bank
- 3- By giving the bill of exchange to the bank , importer gets the permission for import and the right to take the goods from the customs
- 4- The importer takes the goods from the customs
- 5- Importer's bank sends the bill of exchange to exporter's bank or to the exporter
- 6- In maturity the importer makes the payment and the amount is transferred to the exporter's bank and hence to the exporter

**FIGURE V**

**OPEN ACCOUNTS WITH ACCEPTANCE CREDIT FLOW CHART**



Source: Euro Factoring

## **Result**

Open account operations completely depend on trust. Since it is simple and it brings clearness to the parties, it is preferred by most exporters. As far as we accept that all businessmen are trustworthy, open account transactions should be used all the time. However, this is not the case and there is no guarantee of payment by open accounts. Factoring is applied as open accounts, so it offers the exporters the advantages of this method. At the same time, factoring takes upon the risk of non-payment.

## **FACTORING VS. CASH AGAINST DOCUMENTS**

In exports with Cash Against Documents, the importer should get the documents in order to take the goods from the customs. The importer has to make the payment according to the agreement made with the exporter in order to get these documents. This operation can be made by making the payment or by signing a bill of exchange. However, the bill of exchange should be guaranteed by the bank.

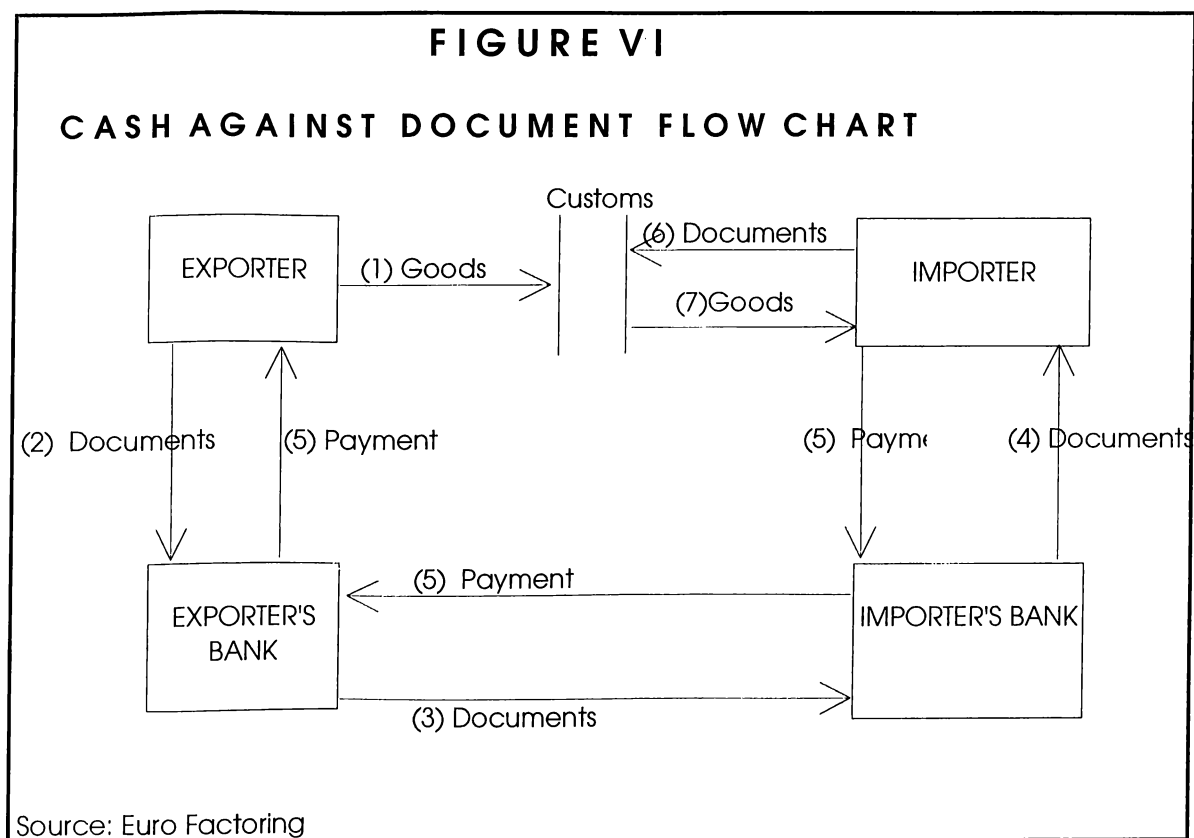
The most important disadvantage for the exporter is that the importer will not get the documents from the bank and hence keep the goods wait in the customs. Since the payment is not done the exporter is faced with difficulties. In addition the importer may not accept the goods and with bad intentions may demand a discount on the price by claiming defect in the goods. The exporter will probably accept the discount since it can not sell the same goods with the same price <sup>1</sup>.

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<sup>1</sup> Doing this brings extra costs for the exporter

As seen in Figure VI Cash Against Documents works as follows:

- 1- Exporter sends the goods
- 2- At the same time, the exporter gives the documents to its bank
- 3- Exporter's bank sends the documents to the importer's bank
- 4-5 The importer makes the payment and gets the needed documents from the bank
- 6-7 The importer takes the goods from the customs after it gets the documents



**Result:**

In this method of export, problems in getting the payments are eliminated in some way: Payment is made in cash or bill of exchange with bank guarantee can be used. However, the main problem is that the goods won't be accepted by the importer and all the risk is borne by the exporter since it did not receive the payments. Exports with open accounts is superior to export with Cash Against Document. Factoring by providing the advantages of export with Open Accounts is superior to both of them.

Buyer will also not prefer this method because the payment is done in cash; not in forward.

**FACTORING VS. EXPORT CREDIT INSURANCE**

Export Credit Insurance is an insurance type which secures the losses of exporters arising from payment difficulties faced by the importer or from some political events. An exporter who wants to use this insurance applies to a bank with a proposal about the transactions it will enter into. After the research made by the bank an insurance policy between the bank and the exporter is signed. The bank sets a limit for each buyer the exporter will enter into transaction. This limit is the maximum amount the bank will pay in case of events arising from the risks determined in the insurance policy.

**Result**

Export Credit Insurance guarantees payments within limits in case of non-payment by the buyer. Factoring has the same advantage too. In addition, the seller can receive %80 of the receivable in 2-3 days time.

## **FACTORING VS. DISCOUNT ON DRAFT**

In banking, discount on draft is a financing method in which the amount in a receipt is paid to the holder before maturity. The interest up to maturity is deducted from the amount to be paid. By the discount agreement made between the bank and the client, the client endorses the deed with the bank and gives the payrolls of the deed to the bank. The bank makes the payment to the client after determining whether the deeds are within the credit limits in the discount agreement and whether the financial positions of the debtors are acceptable. From the amount to be paid the interest up to maturity, expenses and the commissions are deducted.

### **Result**

If the debtors do not pay at maturity, the bank makes a formal protest but does not do anything for the collection of payments. In case that the debt is not paid in maturity the bank has the right to demand payments from the seller. The bank does not bear the risk of nonpayment. However, factors bear all this risk. In addition to the collection of payments factors offer various services to the clients. In contrast, with the Discount on Draft method the bank only makes the formal protest in case of nonpayment.

## **FACTORING VS. CONVEYANCE CREDIT**

Conveyance Credit is a way for the client to satisfy the credit need from a bank by conveying all or part of its receivables as a collateral. Factoring is preferred to Conveyance Credit because in factoring receivables are not conveyed as collateral and factors take all the risks of nonpayment. However, in Conveyance Credit this risk is borne by the firm which conveys its receivables as collateral.

The exporter uses credit from the bank as a stock financing before the export transaction. The exporter creates itself operating capital with this credit. In the balance sheet of the firm, this credit is written as bank debt. This debt fastens the cash flow of the firm and is not a desirable item in the balance sheet. In addition, when the firm needs another loan from the bank it will be harder to get this credit because there is already a risk in the bank. If the same firm conducts its export through factoring, it can use the same loan from the bank and at the same time it will receive the payment of debts through factoring, as a second financing, 2 or 3 days after it shipped the goods. Since the firm is under no obligation because of this second financing, it will not be shown as debt in the balance sheet. Since the firm does not have receivables account, balance sheet will be more liquid.

All the Turkish exporters have to transfer the payments for goods to Turkey in a stated period. The exporter should transfer %70 of this amount in 90 days or %100 of it in 180 days. By using factoring firms can transfer %80 of this amount in 2-3 days time; so they are relieved from this obligation.

## **CHAPTER IV**

### **PROBLEMS OF FACTORING**

In Turkey, factoring has been being implemented since 1980's. After 1992, it has begun to be used widely and the number of factoring firms has increased. Factoring has been implemented according to general rules in most of the European countries and America.

In Turkey, factoring applications are according to the Debts Law under the heading of Conveyance of Receivables. Such regulations were considered to be general because they regulated only the creation and collection of receivables part of the factoring operation. There was no consideration for the details of the factoring operation. Since the number of factoring firms has increased a lot and since domestic factoring is more widely used, these kind of general regulations have become insufficient. As a result, there has been a need for special regulations. With this purpose, with the statutory decree numbered 545 published in 27 June 1995, statutory decree numbered 90 about giving debts is changed. With the statutory decree numbered 545 factoring operations are defined and the right to bring regulations about the subject is given to Undersecretariat of Treasury. Treasury issues the bylaws about the establishment and operations of factoring firms in Turkey.



## **PROBLEMS ARISING FROM REGULATIONS**

Risk management is a service offered by factors. However, this requires the establishment of a wide information base and credit information system. The entrance means to Central Bank Risk Centralization can be a solution to this problem.

Factoring firms pay the Bank-Insurance Transaction Tax when they get credit from the banks. They include this tax in cost of funds. In addition, factors have to include this tax in the invoice given to the client according to the regulations. This means that the client has to pay this tax twice. This increases the cost of factoring and causes a decrease in demand for it. In Turkey, banks do not have to pay this tax. The same right should also be given to the factoring firms.

Factors also pay stamp tax in rate of %6 in their factoring agreements. In order to encourage the sector, factoring firms, as leasing firms, should be exempt from this tax.

It should be accepted that factoring operations is not a banking operation due to Banks Law. By the changes in Banking Law, credit taking should be made more easier and less costly for the factoring firms. Eximbank should give support to factoring firms. If this is done, risks arising from exporting will be kept in foreign countries and it would be possible to operate in countries where factoring does not exist. When factoring has access to Eximbank credit insurance, there will also be increase in Turkish exports. The most important motive in the development of factoring in most countries is the ability of factors to diverge and reassure the risks they take. Since credit insurance is not included among subjects that can be insured in Turkey, Insurance Control Law should be reorganized.

There are different regulations and laws about trade in different countries. This causes many problems in applications of international factoring. It should be the job of FCI to establish an international association to deal with this problem. In an era of globalization standardization of regulations in trade is important. If this is done, there will be a certain increase in the world trade volume.<sup>2</sup>

## **PROBLEMS OF FUNDING**

One of the main problems Turkish factoring firms face is the problem of creation of funds. According to current regulations factoring firms can get credit from banks, in addition to their own capital, to create funds. They use these funds created to give credit to their clients. However, factoring firms should be able to supply the funds that the clients need both in domestic and foreign trade with the widest possibilities. With this respect, factoring firms in Turkey, as the factors in developed countries, should be able to sell treasury bonds and government securities and enter into Interbank as banks. However, factors in Turkey get credit from banks as ordinary firms to conduct their operations. More information about the contents of income, receivables and expenses can be seen in the aggregated balance sheet and income statement of factoring companies in Table III A and Table IV A in the Appendix.

Factors should not pay Bank Insurance Transaction Tax. If they become exempt from this tax, cost of funding will decrease. Moreover, factors should be able to use short term foreign currency credits to support exports. There is no exchange rate risk in this condition because the receipts from the importers will also be in foreign currency. If there is political support, funding problem can be solved. The main actor in solving these problems is the Central Bank of Turkey.

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<sup>2</sup> Both domestically and internationally

With the recent regulations, the minimum capital for factoring firms has been increased to 75 billion Turkish Lira. Also it is stated that factors can not get debts more than 15 times of their capital. With these regulations it is desired that factoring firms become financial firms that create funds for the real economy using their own capital rather than being intermediaries that transfer funds collected from the banking system to firms producing goods and services.

A factoring firm which is recognized as a legal establishment, registered in the Treasury and perceived as a successful company has the chance to issue stocks in the Istanbul Stock Exchange. As mentioned before, factoring firms have two main sources of funding; credits and capital. Issuing stocks provides extra funds for the factors. The cost per \$ raised of issuing stocks is much less than the cost of getting credits. A firm can issue stocks and raise funds which are more than the nominal value of the issue because it will be able to sell the stocks at a higher price. The amount of fund that can be raised depends on the success and the reputation of the factoring firm. The main benefit of issuing stock is that the cost of funding decreases for the factoring firm. This will be reflected in the cost of factoring for the sellers. As a result, more firms will prefer factoring and hence the volume of factoring in Turkey will increase. Stock issue is a new term for the factoring firms. Capital Market Board should help and provide the needed assistance in the issue of stocks in order to make this process easier for the factors. In addition, as mentioned before, exemption from institutional taxes during addition of emission premiums to the firm capital will make it easier for the factoring firm to issue stocks.

### **OTHER PROBLEMS OF FACTORING**

Factoring is not known extensively in the Turkish market. Most of the businessmen think that factoring is a kind of usury. This image of factoring arose from the wrong

applications. Before 1995, people who wanted to supply debts to investors established factoring firms to put their operations in legal framework. After 1995, new regulations have been put to prevent such applications. However, most of the firms are not aware of these developments. These problems can be overcome by communicating the developments in factoring to businessmen.

Meaning and benefits of factoring are not still understood by traders. Most of the potential clients think that factoring is risky although it is less risky in reality. They also think that factoring services are more expensive than alternatives. Factoring firms should learn how to market their products. Detailed brochures about factoring should be printed and sent to businessmen. The target market of firms that need factoring facilities should be determined and introduction of factoring should be concentrated more on them. Government should also help in introduction of factoring because if factoring is used extensively there will certainly be increase in domestic and foreign trade of Turkey.

Education is another problem of factoring in Turkey. There are not enough employees with the needed quality. Most of the students in universities do not know what factoring is. The idea is that courses about factoring should be included in the university curriculum. Most factoring firms try to educate their employees themselves. If this done in universities there will be less burden on factoring firms so that they can concentrate their funds more on their job.

### **FACTORING ASSOCIATION**

Turkish Factoring Association, established in April 1994 by 15 factors, is working to find solutions for the problems of factoring. Although the association is established by factors which have bank relations, any factor which fulfills some requirements can be a

member of this association. In order to be a member the factor should be a legal firm registered in the Undersecretariat of Treasury and it should conduct export factoring in addition to domestic factoring.

The aim of the association is to form standard rules by autocontrol and to find solutions to the problems of the sector. The association conducted with related institutions of government for the formation of regulations and they succeeded in this. With the regulations published in June 27, 1995 a legal framework was established. Factoring Association works with Ministry of Finance for exempting factoring operations from Bank Insurance Transaction Tax and for solutions to other funding problems. Moreover, they are trying to get permission from Council of Ministers to include the association in the world factoring chain.

By the end of 1995, the general secretary of the association is Aydin Dundar. He proposes that they have been partially successful in their attempts to find solutions to the problems. However, they face some problems like bureaucracy and power of competitive financial services. So, it is recommended that more factors become the member of Factoring Association. This way they can have more power and they can guarantee the future of factoring in Turkey. The most effective way to deal with problems is the formation of an organization in the sector.

## **CHAPTER V**

### **CONCLUSION**

Factoring is the transfer of receivables of a firm, which sells goods and services, to a factor and collection of payments for receivables by the factor. The seller speeds up the turnover of receivables into cash and puts its receivables under guarantee since the factor takes the risk of default of payments. The basic functions of factoring are financing, collection of debts, accounting of debts and credit management. These three services are either offered together or with the demand of the clients separately.

Factors Chain International (FCI) is a foundation established by factors in various countries. The aim of FCI is to form a global communication network between factors. The key factor that contributes to the development of FCI is the transfer of know-how and experience from settled factors to ones with less experience. FCI and members help firms to enter into new markets and facilitate trade in present markets.

By the end of 1994, there were 597 factoring firms in the world and the total factoring volume was \$294 billion. The number of factoring firms almost doubled and the total factoring volume increased by %250 in the last decade. In Turkey there are currently 44 factoring firms, and by the end of 1995 total factoring volume has reached up to 13 trillion Turkish Lira while it was around 200 billion Turkish Lira in 1983.

In this study factoring is compared against:

- Letter of Credit
- Open Account
- Open Accounts with Acceptance Credit
- Cash Against Documents
- Export Credit Insurance
- Discount on Draft
- Conveyance Credit

These are the main methods used by the sellers in Turkey to ensure their receipts. The study showed that although each method has its own advantages, factoring is superior to all in today's conditions. The main advantages of factoring are that the risk of default of payments is directly transferred to the factor and that the seller receives up to %80 of payments in a few days time.

Although factoring has many advantages, other alternatives are widely used in Turkey. The reasons of this are:

-Factoring volume is ahead of Letter of Credit, open accounts etc. volume in USA. It has been being used since 1890s' in USA. However, it is a new concept in Turkey. First factoring firm was established in 1988. Turkish firms do not know the advantages of factoring. They still perceive it as a risky and expensive operation. The main reason of this is that factoring firms do not communicate its meaning and advantages to the firms. In addition, Turkish people have a tendency to trust on traditional things. This motive makes them to use the methods that have been used for many years.

- Before, firms were used to sales with cash so there was not much need for services of factoring. However, conditions have changed and buyers now prefer sales in forward.

- Factoring has many problems. These problems make it harder for the clients to realize the benefits of factoring because it can not be implemented effectively and efficiently. This also increases the cost of factoring.

- Each method has some advantages either for the buyer or the seller. For example, cash against documents is advantageous for the buyer because it can keep the goods wait in the customs and then get the chance to buy them at discount. Each party tries to make a contract that is more favorable for itself. So, the decision as to which method will be chosen depends on the relative power of each party. For example, if there is monopsony in the buyer market and high competition in the seller market, the buyers will be more powerful and hence can force the seller to accept cash against document terms.

- Choice of any methods depends on the risk return preferences of the clients. If the risk of default of receivables is low then there will be no need for the services of factoring. The client makes a cost-benefit analysis and decides accordingly.

Although factoring is the most suitable method both for exporters and domestic sellers, it has not been regulated by separate laws in Turkey completely until 1994. It has been implemented due to general rules adopted from USA and European countries. The main problems of factoring are problems arising from regulations, funding problems, marketing problems and lack of needed education.



The development of domestic and export factoring will have positive implications on the Turkish economy. Main benefits of factoring are:

- Factoring helps firms to operate efficiently and productively. By the help of it, firms can concentrate their resources more on production and marketing of products which are their real tasks.
- Firms sell their products in forward but obtain the receipts immediately. In this way, trade in Turkey, production and hence employment improves.
- Factoring is service for sales with invoice. By this way it helps documentation of sales and hence true taxation of money received.
- By the help of factoring, exporters will be less reluctant to enter into new markets and to have new customers. In this way the income from exports will increase. In addition, the open account advantage of factoring will improve the chance of competitiveness of Turkey in foreign markets.
- Factoring operation will help especially for the development of small and medium scale enterprises in Turkey because these kind of firms depend more on their own funding resources and their opportunity to find credits is more limited.

If we want to benefit from these advantages, we should try to solve the problems of factoring. The greater the number of legal factoring firms and the easier it is for them to obtain funds, the more we will gain from factoring operations.

At the beginning of 1996 we have entered into the Customs Union. It is quite probable that we will also be a member of European Economic Community in the near future. This means that Turkish firms will have more opportunity to sell in other countries and they will have to deal with thousands of new firms. Factoring firms will help in utilizing these opportunities.

Factoring operations should not be a banking operation due to Banks Law in credit taking. There is at least a consensus that real factoring does not include a credit operation according to Banks Law. In reality it is wrong to conduct such an operation which has that much functions under the Banks Law.

In the introduction of factoring, marketing gains importance. There are marketing departments in most of the factoring firms in Turkey. Their function is contacting with the customers and telling them the benefits of factoring. However, the people in this department are usually finance oriented people. Marketing people should also be employed in factoring firms. Another alternative is that factoring firms can hire the services of a consulting firm in marketing. Such firms would be helpful in analyzing the target market, in finding effective ways to communicate the benefits of factoring through media; that is in marketing of factoring. If the needs of Turkish SMEs are identified, factoring firms would be able to offer services accordingly. Thus, they can increase the volume of factoring.

I believe that expansion of factoring is inevitable which is fundamentally a good thing for the Turkish economy and for the factoring industry. Government should do everything possible to encourage that growth. It is likely that there will be growth in the confidential invoice discounting business and the factors which provide the full factoring service, without recourse, should set up their campaign to alert potential clients to the

pitfalls of opting for the finance rather than the full service. Also it seems inevitable that the success of factoring industry will undoubtedly attract unwelcome attention from bankers who see the way clear for making a killing on the financial aspects of the transaction without a proper service. In order to overcome such oppositions and other difficulties mentioned, factoring firms should work hard for establishing a good reputation. Public acceptance of factoring is mostly due to the professional approach of these companies.

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# APPENDIX

**TABLE I A**  
**LIST OF MEMBERS OF FCI (August 1995)**

COUNTRY	MEMBERS	COUNTRY	MEMBERS
Argentina *	Gallcia S.A. de Factoring y Trading	Korea	Industrial Bank of Korea
	Heller-Sud Servicios Financieros S.A.		Sam Hee Investment and Finance Corp.
Australia	Scottish Pacific Business Finance Pty. Limited		* Shinhan Investment & Finance Corp.
Austria	Intermarket Factoring AG	Malaysia	Arab-Malaysian Merchant Bank Berhad
Belgium	Ace Factors S.A./N.V.		MBf Factors Sdn Bhd
	Belgo-Factors N.V.	Mexico	* Banamex Factorajc, S.A. de CV
	Cera Factors NV		* Factorajc Bancomer S.A. de CV
Canada	Accord Business Credit Inc.		* Factor Quadrum de Mexico, S.A. de CV
	Royal Bank Export Finance Co. Ltd.	Morocco	* Attijari Factoring Maree
Chile	* Banedwards Factoring Finersa S.A.	Netherlands	FMN Finance House
	Banosomo Factoring S.A.		De Lage Landen Factors B.V.
China	Bank of China	Norway	* Elcon Finans A/S
	Bank of Communications		* FactoNor AS
	Oriental Factors Ltd.		Factoring Finans AS
Cyprus *	Bank of Cyprus (Factors) Ltd.		K-Finans AS
	Laili Factors Ltd.	Philippines *	Development Bank of the Philippines
Czech Rep.	Transfinance Ltd.	Poland	* Polfactor SA
	O.B. Hellers a.s.	Portugal	BNP Factor
Denmark	Forenede Factors A/S	Romania	* Romanian Bank for Development SA
	Nordisk Factoring A/S	Russia	* Tveruniversalbank
Finland	Merita Finance Ltd.		* Mosbusinessbank
France	Banque Sofirec		* Commercial Innovation Bank Alfa Bank
	Factofrance Heller	Singapore	DBS Factors Pte Ltd
	Factorem		* Keppel Factors Pte Ltd
	BNP Factors		OUB Factors Pte Ltd
	UFB Locaball	Slovakia	VUB Factoring as
Germany	Deutsche Factoring Bank	Slovenia *	LB Factors d.d.
	Disko Factoring Finanz GmbH	South Africa	Nedbank
	Gefa		* The Standard Bank of South Africa Ltd
Greece	* ABC Factors A.E.	Spain	Bansabadell Factoring S.A.
	Agricultural Bank of Greece		Catalana de Factoring
	Fact Hellas S.A.		* Heller Factoring Espafola, S.A.
	Ethnofact S.A.		Hispamer Factoring S.A.
Hong Kong	The Hong Kong and Shanghai Banking Ltd		Santander de Factoring S.A.
Hungary *	Hungarian Foreign Trade Bank Ltd.	Sweden	* Handelsbanken Finans AB
	Magyar Factor Kft.	Taiwan	Challcase Finance Co., Ltd
	* Postbank and Savings Bank Corp.	Thailand	* The Siam City Factoring Co. Ltd
Iceland	* Landsbanki Islands	Turkey	Aktif Finans Factoring Hizmetleri
Indonesia	PT. BII Finance Center		* Devir Factoring Hizmetleri AS
	PT Sallindo Perdana Finance		* Euro Factoring Alacak Alimi AS
Israel	* Israel general Bank Ltd.		Factofinans Alacak Alimi AS
Italy	Barclays Factoring S.p.A.		Heller Factoring AS
	* C.B.I. Factor S.p.A.		* Is Factoring Finansman Hizmetleri
	Centro factoring S.p.A.		* Demir Factoring AS
	COFIRI Factor S.p.A.		* Fiba Factoring Hizmetleri AS
	Factorit S.p.A.		* Toprak Factoring AS
	Istituto Bancario San Paolo di Torino S.p.A.	U.K.	Alex Lawrie factors Limited
	Mediofactoring S.p.A.		Barclays Commercial Services
	MontePaschi Factor S.p.A.	*	TSB Factors Limited
Japan	The Central Factors Ltd.		Griffin Factors Limited
	Dai-ichi Kangin Factoring Co. Ltd.		Kellock Limited
	Diamond Factors Ltd.	USA	BNY Financial Corporation
	* Fujigin Factors Limited		The CIT Group/Commercial Services
	Sumigin General Finance Co. Ltd.		NationsBank Commercial Services
Korea	Central Investment & Finance Corp.		Rosenthal & Rosenthal Inc.
	* Cho Hung Bank		* Sun Trust Bank, Atlanta
	* The Commercial Bank of Korea Ltd.		* Heller Financial Inc.
	* Dong-A-Investment and Finance Corp.		* Congress Talcott Corporation

\* Associate Members

Source: Dunya, September 1995

**TABLE II A****INFORMATION ABOUT FACTORING COMMISSIONS**

<b>WEIGHTED AVERAGE FACTORING INTEREST RATE ANNUAL (%)</b>	<b>TL</b>	<b>Foreign Exchange</b>		
		<b>\$</b>	<b>DM</b>	<b>Other</b>
	91	8	7	8
<b>WEIGHTED AVERAGE COMMISSION RATE (%)</b>	<b>Domestic</b>	<b>Export</b>		
		<b>\$</b>	<b>DM</b>	<b>Other</b>
	1	1	1	2
<b>AVERAGE MATURITY (Day)</b>	<b>Domestic</b>	<b>Export</b>		
		<b>\$</b>	<b>DM</b>	<b>Other</b>
	54	61	64	63
<b>AVERAGE ADVANCE RATE</b>	<b>Domestic</b>	<b>Export</b>		
		<b>70</b>		
	82			
<b>AMOUNT OF CHECKS AND PROMISORY NOTES RECEIVED AS GUARANTEE ( MILLION TL)</b>	<b>Checks</b>	<b>Promissory Notes</b>		
	7,404,930	1,417,857		

Source: Undersecretariat of Treasury



**TABLE III A**  
**AGGREGATED BALANCE SHEET OF FACTORING COMPANIES**

	1995/II	1995/III		1995/II	1995/III
<b>ASSETS</b>			<b>LIABILITIES</b>		
<b>I. CURRENT ASSETS</b>	<b>14,106,584</b>	<b>19,588,502</b>			
CASH ITEMS	912,493	1,682,894	<b>III. SHORT TERM LIABILITIES</b>	<b>8,047,001</b>	<b>10,581,818</b>
SECURITIES PORTFOLIO	873,667	1,204,213	Borrowing from Banks	4,161,887	4,938,499
Stocks	127,976	178,291	TL	2,270,597	2,777,490
Private Sector Bills and Bonds	0	1,511	FX	1,891,290	2,161,009
Public Sector Bills and Bonds	736,183	1,017,773	Interests and Principles to be paid for Long Term Borrowings	621,838	684,496
Other	10,718	19,000	Interests and Principles to be Paid To Issued Bonds	141,581	176,700
Provisions for undervalued securities	1,210	12,365	Issued Bonds and Bills	133,442	176,660
FACTORING RECEIVABLES	11,761,006	15,712,399	Other Issued Securities	0	0
Domestic	8,809,906	11,828,914	Other	4	15
Export	2,353,501	3,127,740	ACCOUNT PAYABLE TO FACTORED CLIENTS	2,389,464	3,686,074
Import	412,858	530,608	Domestic	1,002,329	1,848,184
Overdue Factoring Receivables	299,914	382,200	Export	1,019,423	1,307,467
Provisions	145,206	157,063	Import	337,713	530,123
OTHER RECEIVABLES	244,326	536,865	OTHER SHORT TERM BORROWINGS	178,768	367,245
SHORT TERM PREPAID EXPENSES AND INCOME ACCRUALS	196,508	328,465	TAX and OTHER COMMITMENTS TO BE PAID	131,486	105,928
OTHER CURRENT ASSETS	118,585	123,666	PROVISIONS FOR DEBT AND COSTS	137,817	274,671
<b>II. FIXED ASSETS</b>	<b>1,962,144</b>	<b>2,769,088</b>	SHORT TERM ACCRUED EXPENSES	147,814	171,529
FINANCIAL FIXED ASSETS	1,620,879	2,197,542	OTHER SHORT TERM LIABILITIES	0	0
TANGIBLE FIXED ASSETS (Net)	88,421	176,807	<b>IV. LONG TERM LIABILITIES</b>	<b>4,333,192</b>	<b>6,425,095</b>
INTANGIBLE FIXED ASSETS	237,733	345,204	FINANCIAL BORROWINGS	3,696,817	6,374,363
LONG TERM PREPAID EXPENSES and INCOME ACCRUALS	3,552	39,128	Borrowing From Banks	3,590,623	5,818,976
OTHER FIXED ASSETS	11,558	10,407	TL	371,823	262,372
<b>TOTAL ASSETS</b>	<b>16,068,727</b>	<b>22,357,590</b>	FX	3,218,800	5,556,601
			Issued Bills and Bonds	100,000	100,000
			Other Issued Securities	0	0
			Other	6,224	455,387
			OTHER LONG TERM BORROWING BORROWINGS	578,857	1,054
			LONG TERM PROVISIONS FOR DEBT AND COSTS	8,360	8,412
			LONG TERM ACCRUED EXPENSES	49,129	41,266
			OTHER LONG TERM LIABILITIES	0	0
			<b>V. NETWORTH</b>	<b>3,688,534</b>	<b>5,350,676</b>
			PAID IN CAPITAL	2,631,850	3,167,100
			RESERVES	330,090	255,432
			REVALUATION FUNDS	96,849	463,371
			RETAINED EARNINGS	16,182	12,941
			LOSS FROM PREVIOUS TERMS	128,654	129,709
			NET PROFIT (Loss)	712,217	1,281,511
			Net Profit	770,157	1,314,966
			Net Loss	27,310	33,425
			<b>TOTAL LIABILITIES</b>	<b>16,068,727</b>	<b>22,357,590</b>

**TABLE IV A**  
**AGGREGATED INCOME STATEMENT OF FACTORING COMPANIES**

	1995/II	1995/III
<b>FACTORING INCOMES</b>	<b>2516871</b>	<b>4589802</b>
Factoring Interest Income	2333620	4246207
-Domestic	2231388	3914187
-Export	102233	332020
Factoring Commission Received	183250	343595
-Domestic	133740	258497
-Export	42508	74757
-Import	7002	10342
<b>OPERATION EXPENSES</b>	<b>320175</b>	<b>535808</b>
ORDINARY INCOMES FROM OTHER TRANSACTIONS	1100872	1794994
ORDINARY EXPENSES AND LOSS FROM OTHER TRANSACTIONS	832081	1625563
<b>BORROWING COSTS</b>	<b>1672575</b>	<b>2850420</b>
Short Term Borrowing Costs	1167268	1905205
Interest Expenses Paid for Banks' Credits	1149895	1878598
Interest Expenses Paid to Issued Securities	17373	26607
Short Term Borrowing Costs	505307	945214
Interest Expenses paid for Banks' Credits	320755	629798
Interest expenses Paid to Issued Securities	184552	315416
EXTRAORDINARY INCOME AND PROFIT	48645	65048
EXTRAORDINARY COSTS AND LOSS	1667	12417
<b>PROFIT/LOSS</b>	<b>839890</b>	<b>1425636</b>
PROVISIONS FOR TAX AND OTHER LEGAL COMMITMENTS TO BE PAID	97673	144094
<b>NET PROFIT/LOSS</b>	<b>742217</b>	<b>1281541</b>